Testimony of JPMorgan Chase

Senate Appropriations Subcommittee on Financial Services and General Government United States Senate

December 4th, 2008

Chairman Durbin and Members of the Subcommittee on Financial Services and General Government, we appreciate the opportunity to appear before you today on this most important topic of helping homeowners. We recognize that no one benefits in a foreclosure.

My name is Molly Sheehan and I work for the Home Lending Division of JPMorgan Chase as a senior housing policy advisor. Chase is one of the largest residential mortgage servicers in the United States, serving over 10.5 million customers on the platforms of Chase, WaMu and EMC, with mortgage and home equity loans of approximately $1.5 trillion in every state of the country. We are proud to be part of one of this country's pre-eminent financial institutions with a heritage of over 200 years.

Chase services about $335 billion in mortgages and home-equity loans it owns; that's $181 billion (12% of total serviced) in first-lien mortgage loans and about $154 billion in home equity (10% of total serviced). It also services or sub-services more than $1.166 trillion (78% of total serviced) in first-lien mortgage loans owned by investors. In the combined $1.5 trillion portfolio, there is $144 billion (10%) of non prime: $23 billion owned by Chase and $121 billion owned by investors. Pay option ARMs are 9% of the total serviced portfolio, with $50 billion owned by Chase and $74 billion owned by investors. Chase inherited pay option ARMs when we acquired WaMu's mortgage portfolio in late September and EMC's portfolio earlier this year as part of the Bear Stearns acquisition.

As you know, we recently announced several significant enhancements and we would like to share those with you.

Expanded Foreclosure Prevention Initiatives

While Chase has helped many families already, we feel it is our responsibility to provide additional help to homeowners during these challenging times. We will work with families who want to save their homes but are struggling to make their payments.

That's why we announced on October 31st that we are undertaking multiple new initiatives designed to keep more families in their homes.

We will open regional counseling centers, hire additional loan counselors, introduce new financing alternatives, proactively reach out to borrowers to offer pre-qualified modifications, and commence a new process to independently review each loan before moving it into the foreclosure process. We expect to implement these changes within the next 60 days.

While implementing these enhancements, we have stopped any additional portfolio loans from entering the foreclosure process. This will give potentially eligible homeowners an opportunity to take advantage of these enhancements, and applies to owner-occupied properties with mortgages owned by Chase, WaMu or EMC, or with investor approval. Chase has worked diligently and will continue to work diligently with investors to apply these enhancements to loans we service on behalf of others so our efforts can have the broadest possible impact. We also will advise homeowners in the foreclosure process to continue to work with their assigned counselors who will have access to our expanded range of modification alternatives.

The enhanced program is expected to help an additional 400,000 families – with $70 billion in loans – in the next two years. Since early 2007, Chase, WaMu and EMC have helped about 250,000 families avoid foreclosure, primarily by modifying their loans or payments. The enhanced programs apply only to owner-occupied properties.

We inherited pay-option ARMs when we acquired WaMu's mortgage portfolio in late September and EMC's portfolio earlier this year as part of the Bear Stearns acquisition. After reviewing the alternatives that were being offered to customers, we decided to add more modification choices. All the offers will eliminate negative amortization and are expected to be more affordable for borrowers in the long term.

As a result of these enhancements for Chase, WaMu and EMC customers, Chase will:

· Systematically review its entire mortgage portfolio to determine proactively which homeowners are most likely to require help – and try to provide it before they are unable to make payments.

· Proactively reach out to homeowners to offer pre-qualified modifications such as interest-rate reductions and/or principal forbearance. The pre-qualified offers will streamline the modification process and help homeowners understand that Chase is offering a specific option to make their monthly payment more affordable.

· Establish 24 new regional counseling centers to provide face-to-face help in areas with high delinquency rates, building on the success of one- and two-day Hope Now reach-out days. We will partner with our community counselors to reach more borrowers.

. Add 300 more loan counselors – bringing the total to more than 2,500 – so that delinquent homeowners can work with the same counselor throughout the process, improving follow-through and success rates. Chase will add more counselors as needed.

· Create a separate and independent review process within Chase to examine each mortgage before it is sent into the foreclosure process -- and to validate that the homeowner was offered appropriate modifications. Chase will staff the new function with approximately 150 people.

· Not add any more Chase- owned loans into the foreclosure process while enhancements are being implemented.

· Disclose and explain in plain and simple terms the refinancing or modification alternatives for each kind of loan. Chase also will use in-language communications, including local publications, to more effectively reach homeowners.

. Expand the range of financing alternatives offered to modify pay-option ARMs to an affordable monthly payment, including 30-year fixed-rate loans, interest rate reductions, principal deferral, and interest-only payments for 10 years. All the alternatives eliminate negative amortization.

· Offer a substantial discount on or donate 500 homes to community groups or through non-profit or government programs designed to stabilize communities.

· Use more flexible eligibility criteria on origination dates, loan-to-value ratios, rate floors and step-up features.

The enhancements reflect Chase's commitment to continue to seek additional ways to help homeowners.

Expanded Offers for ARM Customers

Chase offers two programs for unsolicited rate modifications for short-term hybrid ARMS (2, 3). These programs are specifically designed to avoid delinquency and reward current borrowers who have demonstrated a willingness and ability to pay but may be subject to future payment shock.

- In late 2007, we began a blanket loan modification program for Chase-owned loans. It works very simply for homeowners: We unilaterally lock in the initial interest rate for the life of the loan on all short-term ARMs that are due to reset in the coming quarter. This saves homeowners hundreds of dollars a month. We also have done similar blanket modification programs for investors at their request. Fewer than 10% of these modified loans end up in re-default. We are currently reviewing the EMC and WaMu portfolios to see if this program should be expanded.

- In early 2008, we kicked off the American Securitization Forum (ASF) Fast Track loan modification program for non-prime, short-term hybrid ARMs serviced by us. ASF developed a systematic, highly streamlined process that quickly freezes the loan's current interest rate for five years, protecting the borrower from rate and payment increases. WaMu and EMC also use the ASF Fast Track procedures.

Chase also provides loan modifications for customers who can not sustain their current payment due to affordability. As a general rule, an analysis is completed to determine an affordable payment level for the customer that will result in a reasonable housing ratio (principal, interest, taxes and insurance and condo or association fees as a percentage of income) while producing a more positive result for the investor than foreclosure. Income is subject to verification. WaMu and EMC presently use a net present value (NPV) and affordability model to determine the optimal modification for the borrower and investor. Chase is reviewing that model to determine which approach yields the most consistent and efficient process across all the portfolios.

Chase has had a proactive outreach program for resetting ARM customers since the first quarter of 2007, with no restriction based on origination date. The outreach is done for all

ARM customers with contacts occurring 120 days and 60 days before reset. Under WaMu's Program for option ARMs, starting in January 2008, customer contact begins for all option ARM customers up to 180 days before reset to explore workout and refinance options. EMC has a similar program of outreach that they started in the fourth quarter of 2007, beginning outreach up to 270 days before reset.

Also, as we announced, we will proactively reach out to homeowners to offer pre-qualified modifications such as interest-rate reductions and/or principal forbearance. The pre-qualified offers will streamline the modification process and help homeowners understand that Chase is offering a specific option to make their monthly payment more affordable.

New Offers for Option ARM Customers

Chase did not originate or purchase option ARMs but has acquired portfolios of Option ARMs as a result of its acquisition of EMC and WaMu loans.

WaMu began a proactive program for its owned Option ARM portfolio in January of 2008. Nine months later, WaMu kicked off a more aggressive campaign with more refined targeting and offers for borrowers due to recast in the next 180 days. The offer – and the frequency of follow-up mailings -- depends on whether the consumer is coming up on a scheduled recast or a forced recast. Under the WaMu and EMC programs, the first offer is a refinance into an Agency or FHA loan, including FHASecure. Borrowers can also be referred directly to loss mitigation counselors at their request.

Under the expanded initiatives we recently announced, our second offer for Pay Option ARMs will be a modification to a 30-year fixed-rate fully amortizing loan with elimination of the negative amortization feature. In addition, terms may be extended to as long as 40 years to increase affordability. The interest rate can be reduced as low as 3% to achieve affordability. If a below-market rate is required, the loan rate will begin to step up to a market rate after three years with any adjustments capped at one percent every year to eliminate payment shock. If needed, principal can be deferred down to as low as 90- 95% of the current loan-to-value.

The third offer is a ten-year/interest only ARM at a discounted rate with a floor of 3% and no modification fees. Negative amortization is eliminated. Principal deferral will also be used to as low as a 90 -95% current loan-to-value ratio if required. If a below-market rate is required, the loan rate will begin to step up to a market rate after three years with adjustments capped at one percent every year to eliminate payment shock. This program is designed for home owners who want to stay in their home, so it is limited to owner occupants.

Once operational at Chase, the FHA Hope for Homeowners Program will provide an additional option for these borrowers. We were pleased that HUD announced several modifications to the H4H Program because we believe those changes should expand the number of borrowers we will be able to reach and reduce the operational complexity of offering the product.

For these loan modification programs, we will determine affordability based on a housing ratio (principal, interest, taxes, insurance and condo or association fees) that generally does not exceed a range of 31% to 40%, based on income. Borrowers with housing ratios between 40% and a hard cap of 50% may be eligible if they demonstrate documented compensating factors, which can include the amount by which the monthly payment has been reduced and payment history during the trial modification period. These ratios are being used today by Chase in its current modification programs and their reasonableness has been validated by the relatively low level of recidivism. An NPV analysis will be used to evaluate refinance and modification offers including, in both cases, potential principal deferral. There is no interest charged on the principal forbearance, but a required payment upon sale or refinance allows the owner of the loan to share in any potential future appreciation.

Once borrowers provide preliminary income information, they begin making a reduced payment. But the final modification will be subject to the borrower making up to three consecutive payments at the modified amount as well as receipt and validation of income information and confirmation of current collateral value. No modification fees will be charged and delinquency fees will be waived.

As announced, we anticipate being able to implement the program over the next two months and we will not commence foreclosure proceedings for potentially eligible borrowers for loans owned by Chase and seek investor consent, where required, for serviced loans. Our Project Team has been formed and is working on each of the announced initiatives and we are making significant progress toward our goal of implementing all of them across our portfolio by Jan. 31. As part of that process, we have formed a team to focus on our investors and are developing our outreach strategy to bring these enhancements to loans we service on behalf of investors. Our efforts then can have the broadest possible impact. Once we are able to tangibly demonstrate the methodology and the process, we believe our investors will become comfortable as we roll the program out more broadly and provide any consent that may be needed in particular cases.

We also believe that with the efforts of many servicers, the sharing of best practices and the leadership of the FDIC and the GSEs, the industry is starting to converge on a new industry standard for loan modifications. To the extent the investor community joins in accepting this emerging standard that will provide greater certainty to the servicing industry.

We applaud the announcement by FHFA, Fannie Mae and Freddie Mac of their Streamlined Modification Program (SMP). This Program will bring needed simplicity and consistency to loans being modified in the GSEs' portfolios and securities. While the SMP only applies to loans that are delinquent for more than ninety days, it is still an important step forward. We encourage the FHFA and the Agencies to consider expanding the SMP to also address the needs of homeowners that are current but where default is reasonably foreseeable, based on the borrower's financial profile and the terms of their loan.

The SMP is being implemented by servicers that are part of the HOPE Now Alliance for Agency loans they service. HOPE Now servicers and the GSEs have been working closely with a target date of mid-December to develop the procedures and protocols that servicers will need to implement the SMP. This new initiative will supplement the loan modification efforts of all HOPE Now servicers who have prevented almost 2.7 million foreclosures since the Alliance began reporting in July 2007. The GSEs have announced a freeze on new foreclosure sales during this implementation period. Director Lockhart of the FHFA is calling on the private investor community to adopt the SMP model – a development that would further enhance the effectiveness of the SMP and further reduce foreclosures.

We are pleased to provide this information to you and we will be happy to meet with you and respond to additional questions you may have or ideas you would like to share. In turn, as we continue to improve or programs and efficiency, we would be happy to keep you advised. We especially appreciate your leadership and that of Subcommittee members in keeping a focus on this important issue of keeping families in their homes.